

Commonwealth of Kentucky Personnel Cabinet

Blue Ribbon Panel - Cost Projection Analysis
July 8, 2005



Table of Contents

- Cost Projection Overview
- Comparison Against Prior Projection
- Key Assumptions
- Administrative Expense Components

Cost Projection Overview

Purpose

- Provide an actuarial estimate of the expected increase from the CY2005 fully-insured premiums to CY2006 under a self-insured medical and prescription drug plan.
- This increase estimate maintains the current plan options and designs.

Expected Cost Increase

- Expected increase in total (Commonwealth + EE) costs from 2005 to 2006 (Note: does not reflect RFP responses): **19.3%**

Key Assumptions

- | | |
|------------------------------------|---------------------------------|
| • Administrative Expense Load | • 2006 Plan Enrollment |
| • Health Care Trend (Inflation) | • 2006 Plan Design |
| • Incurred But Not Reported Claims | • 2004 versus 2005 Plan Designs |
| • Stop-Loss Coverage | • 2004 claims experience |

Comparison Against Prior 2006 Cost Estimate

	Cost Estimate with No Changes	Cost Estimate with Changes
% Increase 2005 to 2006	32.0%	19.3%
Basis of Cost Estimate	Used for purposes of assessing appropriateness of moving to self-insured basis	Used for budget purposes
Claims Experience Detail	Aggregate level only	Detailed data reviewed
Insured Status	Fully-insured	Self-insured
Treatment of 2005 Deficits	Carriers would attempt to recoup and Commonwealth would honor request	No recoupment

Key Assumptions: Administration

Key assumptions related to administrative fees:

- Based on 2004 competitive “transparent” administrative bids for similarly sized groups and similar plan types under a self-insured arrangement.
- Assumed trend on administrative fees of 5% per year.
- Administration translates to an approximate 9% load on expected claims.
- Administrative fees include costs related to:
 - **Claims adjudication**
 - **PPO network access**
 - **Medical management services**
 - **FSA administration**
 - **COBRA administration**
 - **HIPAA administration**
 - **Education / decisions support**
 - **Appeals services**
 - **Claims fiduciary responsibility**
 - **Policy conversions**
 - **Wellness programs**
 - **Maternity management**
 - **Billing, underwriting, actuarial**
 - **Legal services**
 - **Drug transaction & dispensing fees**
 - **Communication & implementation**

Key Assumptions: Health Care Trend (Inflation)

Key assumptions related to health care trend:

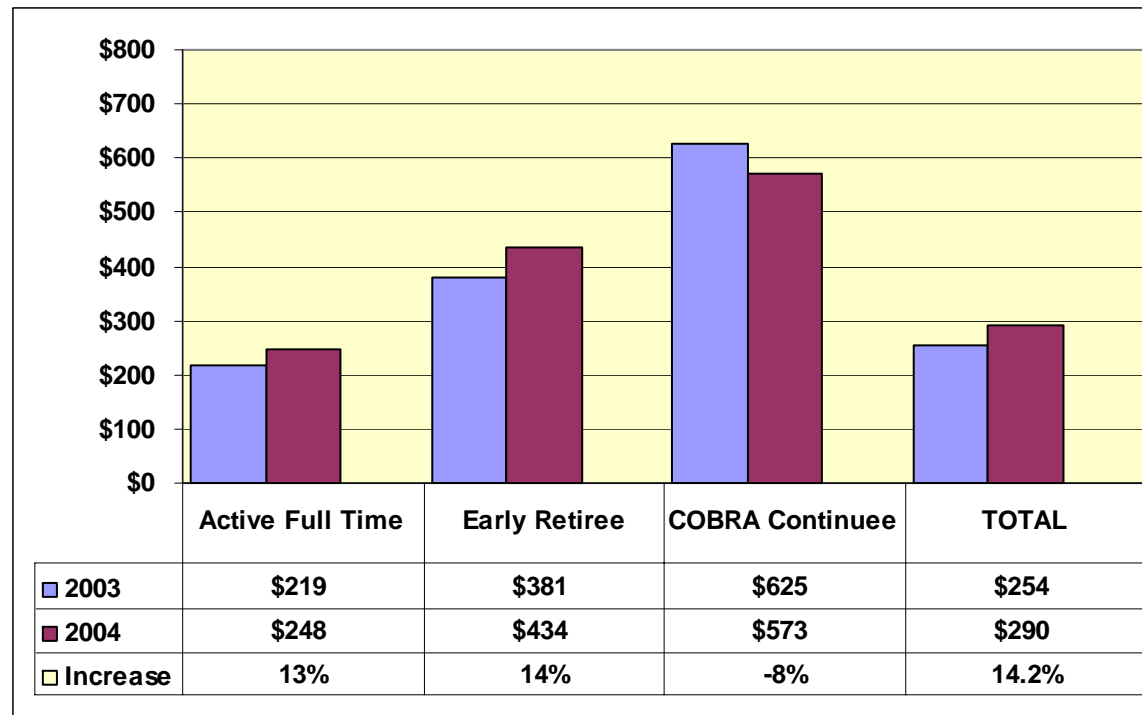
- Annual trend of 15.5% (blended between medical and prescription drugs).
- Based on expected 2004 to 2005 and 2006 national surveys on medical PPO and prescription drug benefits.
- Adjusted for actual Commonwealth experience 2003 to 2004 compared against national surveys 2003 to 2004.
- Reflects expected increase in utilization resulting from richer benefit levels in 2005 compared to 2004.
- The demographics of the covered members also lends itself to recognition of higher trend:
 - Higher than national norm average age (Commonwealth average age of 46 versus national norm average age of 40)
 - The retention of a growing population of early retirees (21% of members)

Key Assumptions: Health Care Trend (Inflation) 2003-2004 Claims Trend

	Commonwealth	Benchmark ¹
Medical: Hospital Inpatient	12.2%	
Medical: Hospital Outpatient	19.3%	
Medical: Physician	11.0%	
Medical: Emergency Room	14.9%	
Medical: Total	14.0%	13.5%
Pharmacy	15.3%	18.1%
Overall	14.2%	14.4%

¹ Segal 2004 healthcare trend survey.

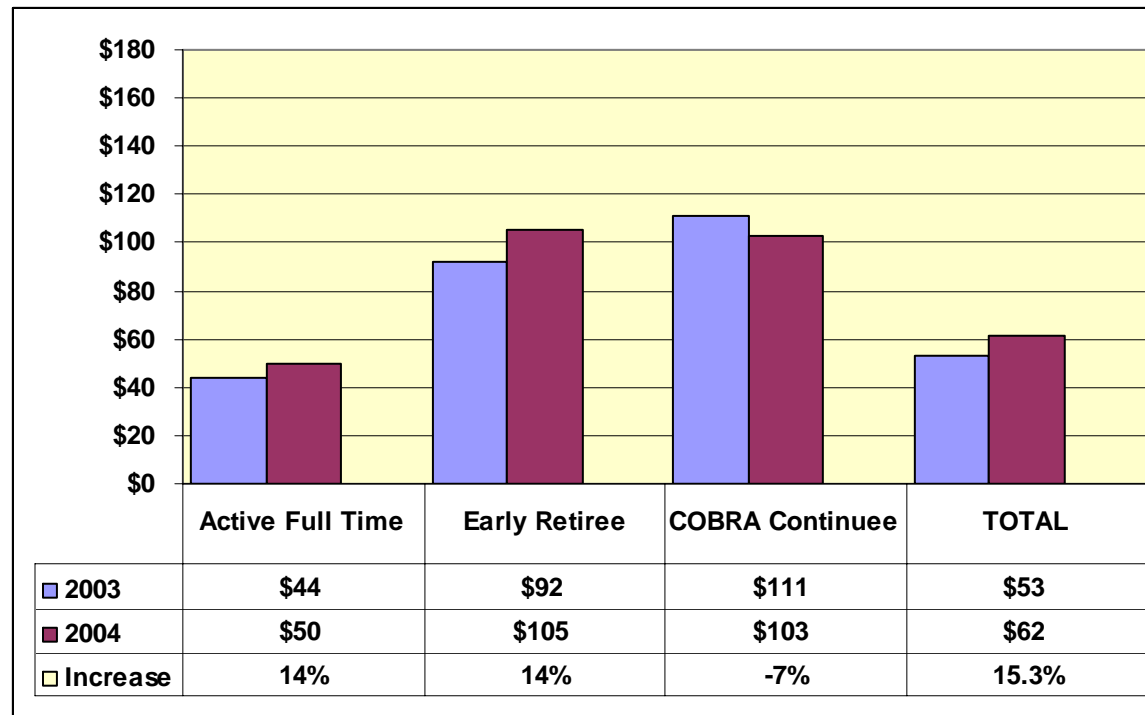
Key Assumptions: Health Care Trend (Inflation) Total (Medical and Pharmacy) Net Plan Paid PMPM



- In 2004, early retiree claims are approximately 1.8 times that of actives.
- In 2004, COBRA claims are approximately 2.3 times that of actives.
- There was overall movement from the active group to the early retiree group from 2003 to 2004. Thus the mix of lives 2003 to 2004 changed.

Key Assumptions: Health Care Trend (Inflation)

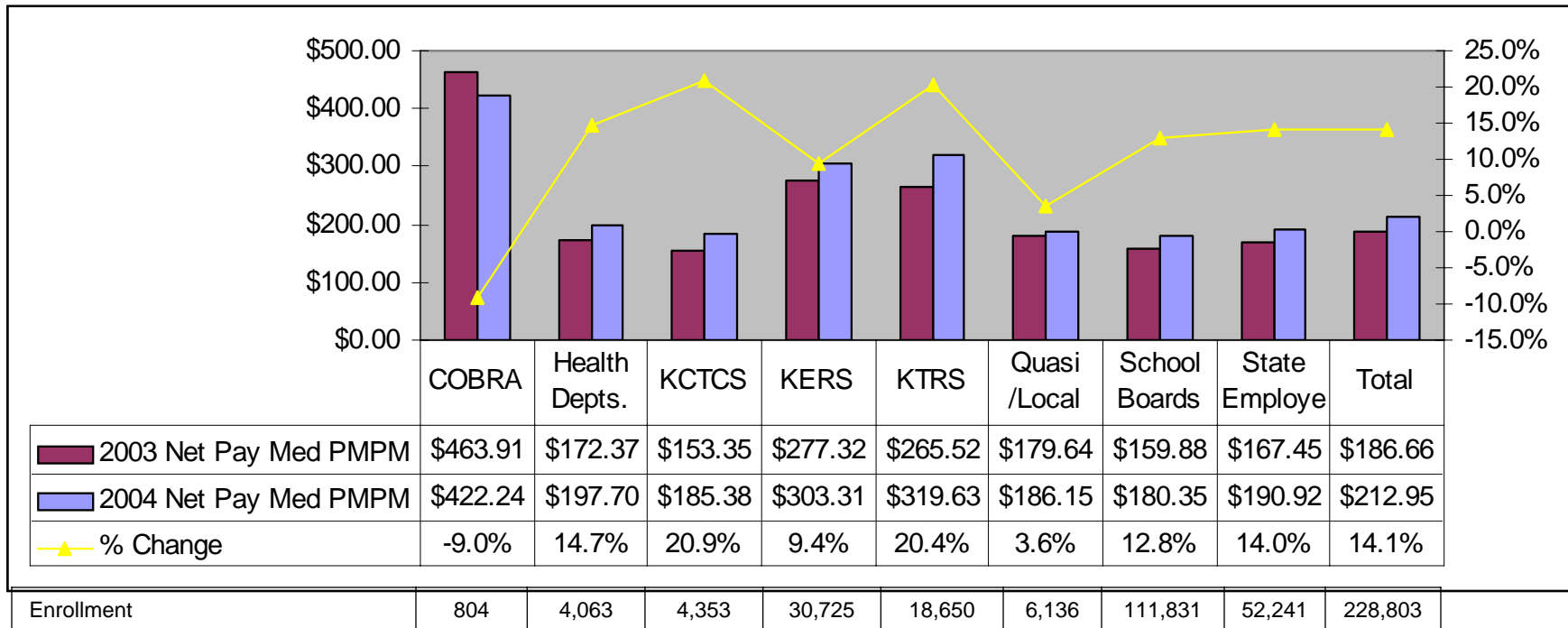
Pharmacy Net Plan Paid PMPM



- In 2004, early retiree claims are approximately 2.1 times that of actives.
- In 2004, COBRA claims are approximately 2.1 times that of actives.
- There was overall movement from the active group to the early retiree group from 2003 to 2004. Thus the mix of lives 2003 to 2004 changed.

Key Assumptions: Health Care Trend (Inflation)

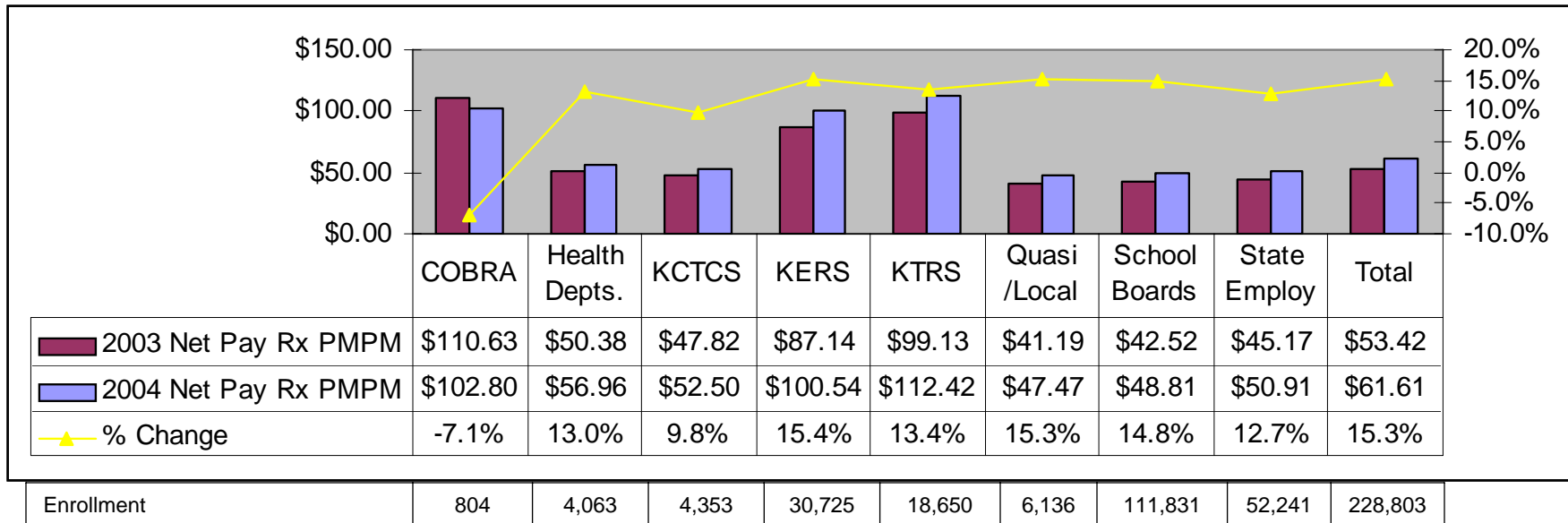
Medical Net Plan Paid PMPM by Group



Above does not include claims coded "missing/other" for group type.

Key Assumptions: Health Care Trend (Inflation)

Pharmacy Net Plan Paid PMPM By Group



Above does not include claims coded "missing/other" for group type.

Key Assumptions: 2004 Claims Experience

Key assumptions related to claims experience used:

- Calendar year 2004 claims experience used.
- 1Q2005 claims experience available, but deemed not yet credible:
 - Paid claims data for 1Q2005 includes runout for 2004.
 - Claims incurred in 2005 and paid 1Q2005 exclude IBNR, which is difficult to estimate based on the limited experience under the new plan designs.
 - Members are still meeting deductibles during 1Q2005, resulting in 2005 experience that is, on an average monthly basis, less than what will ultimately emerge for 2005.

Key Assumptions: IBNR

Key assumptions related to incurred but not reported (IBNR) claims:

- Based on Commonwealth experience.
- Claims experience adjusted by +2.6% to recognize IBNR claims.

Key Assumptions: Stop-Loss Coverage

Key assumptions related to stop-loss coverage:

- No specific or aggregate stop-loss coverage has been assumed in the development of the 2006 cost estimates.

Key Assumptions: 2006 Plan Enrollment

Key assumptions related to plan option enrollment in 2006:

- Assumed to match that in 2005.

Key Assumptions: 2006 Plan Design

Key assumptions related to the plan options in 2006:

- Plan provisions assumed to remain unchanged from 2005.
- “Plan provisions” include such things as deductible, copays, coinsurance, but does not include contribution levels (a funding issue).

Key Assumptions: 2004 v. 2005 Plan Designs

Key assumptions related to change in plan designs from 2004 to 2005:

- Claims estimates based on 2004 experience have been adjusted for changes in plan designs from 2004 to 2005.
- Actual 96% in-network versus 4% out-of-network claims utilization reflected in assessing expected claims changes 2004 to 2005.
- Assumed relative plan design differences include changes in benefit provisions (deductibles, copays, coinsurance, etc.), recognition of discounts, levels of managed care, actual 2004 Commonwealth in-network versus out-of-network utilization, but does not include employee contribution levels.

Key Assumptions: 2004 v. 2005 Plan Designs

This is a comparison of plan “value”, not plan costs.

- 2004 average benefit value based on enrollment: 0.995
- 2005 average benefit value based on enrollment: 1.014
- 2004 to 2005 increase in benefit value: **1.9%**

- 2004 average Commonwealth subsidy: 69.1%
- 2005 average Commonwealth subsidy: 81.1%
- 2004 to 2005 average increase in subsidy: **17.4%**

- 2004 to 2005 benefit & subsidy change in value: **19.6%**